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The Sixth Amendment and Expert Witnesses in Criminal Tax Cases

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Recently, in the *Baxter* case, a federal district court vacated the sentence imposed as a result of a guilty plea in a criminal tax case. The court held that the failure of defense counsel to retain the services of an expert in tax crimes sentencing violated the defendant's Sixth Amendment right to effective representation.[1]

This installment of the Tax Crimes column explores *Baxter*. Part A briefly notes the civil and criminal tax contexts in which tax experts are used. Part B describes *Baxter* and its holding. Part C asks whether defense counsel in criminal tax cases should always retain a tax expert. The *Baxter* court answered this question in the negative. This answer surely is correct. However, *Baxter* was not a remarkably complicated case as far as criminal tax prosecutions go. If retaining an expert was constitutionally required in *Baxter*, doing so may be required in more cases than some attorneys may previously have realized.

A. Experts in Civil and Criminal Tax Cases

Expert witnesses opining about valuation and other matters of fact are frequent participants in tax trials and other kinds of cases.[2] But *Baxter* dealt with the role of experts in matters of law, not fact. Experts on the law are used in three main contexts in tax cases: (1) as testifying witnesses in tax malpractice cases, opining about damages and the accepted standard of care; (2) as testifying witnesses in both civil and criminal cases, opining about tax liability; and (3) as nontestifying consultants in both civil and criminal tax cases.

In some cases, Federal Rule of Evidence 702 stands as a barrier to the admission of expert testimony regarding the law. That rule provides that expert evidence must help the trier of fact to understand the evidence. Judges are, or are presumed to be, experts in the law. Thus, some judges believe that, at least under routine circumstances, expert testimony about the content of the law invades the province of the judge, would not be helpful to the court, and so is inadmissible under rule 702.[3]

The complexity of sentencing has created a demand for expert assistance in criminal tax cases:

> A cadre of lawyers around the country have become known as sentencing experts and are often associated to assist in the sentencing of major cases. . . . Since most tax attorneys rarely handle criminal cases, and since most criminal tax attorneys have little experience with the process of sentencing and incarceration . . . considering the use of a consultant who specializes in sentencing issues sometimes makes good sense.[4]

B. *Baxter*

1. Facts. Laura Baxter worked as a CPA with her own practice. Bruce and Tammy Groen were among her clients. For several years, Baxter had prepared income tax returns for the Groens and for the Groens' several trusts. The Groens, as well as some of Baxter's other clients, participated in bogus trusts purchased from the Aegis Co., which were illegal tax evasion schemes.[5]

In 2004 Baxter was indicted on 11 counts of federal criminal income tax violations pertaining to conduct between 1994 and 1999. A plea deal was reached under which Baxter pled guilty to a one-count superseding information charging her with obstructing administration of the tax laws in violation of section 7212(a). She admitted in the plea agreement and in open court that on October 29, 1997, she submitted a false document to an

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[1] *Baxter v. United States*, 2009 WL 1809927 (N.D. Ill. June 25, 2009), *Doc 2009-14910*, *2009 TNT 124-48*. For additional analysis of *Baxter*, see John Townsend's blog at http://federaltaxcrimes.blogspot.com/2009/06/check-tax-loss-numbers-tale-of.html.

[2] *See generally* Joni Larson, "Tax Evidence II: A Primer on the Federal Rules of Evidence as Applied by the Tax Court," 57 *Tax Law.* 371, 453-468 (2004); Burgess J.W. Raby and William L. Raby, "Reasonable Compensation, Expert Witnesses, and the Tax Practitioner," *Tax Notes*, Sept. 15, 2003, p. 1415, *Doc 2003-20121*, or *2003 TNT 175-30*; Raby and Raby, "Tax Practitioners as Expert Witnesses," *Tax Notes*, Apr. 29, 2002, p. 731, *Doc 2002-9862*, or *2002 TNT 78-33*.

[3] *E.g.*, *Stobie Creek Investments LLC v. United States*, 81 Fed. Cl. 358 (2008), *Doc 2008-5274*, *2008 TNT 49-13* (excluding expert reports proffered in a civil tax shelter case).

[4] John A. Townsend, Larry A. Campagna, Steve R. Johnson, and Scott A. Schumacher, *Tax Crimes*, 411 (2008).

[5] *Baxter*, 2009 WL 1809927, at *1.

IRS revenue agent regarding gain realized by the Groens from the sale of business assets in 1995.[6]

As is typical of tax crimes, the amount of the tax loss was a key component of the sentencing calculation.[7] In the plea agreement, Baxter agreed for sentencing purposes that the tax loss involved exceeded $550,000 but was less than $950,000. The government asserted, but Baxter disputed in the agreement, that the tax loss was $5.1 million (later raised to $5.5 million). The government based this contention on its belief that Baxter had criminally participated in a protracted endeavor to impede tax administration concerning her clients who bought Aegis trust systems.[8]

The parties agreed that the 1995 U.S. Sentencing Guidelines Manual would apply for Baxter's sentencing. In the presentencing report,[9] the probation officer recommended a total offense level of 17, producing a sentencing guidelines range of 24 to 30 months. This was predicated on a tax loss of $576,000 per the plea agreement. The presentencing report rejected the government's tax loss figure of more than $5 million, use of which would have raised the sentencing guidelines range above the statutory maximum of 36 months.[10]

The government objected to the presentencing report's rejection of its tax loss figure. The court held an evidentiary hearing, after which it ruled that the government had not met its burden of showing by a preponderance of the evidence[11] that Baxter had sought to assist in defrauding the United States through the Aegis system. The only criminality conceded by Baxter or proved by the government was her tendering of the false document on October 29, 1997. The court ruled that, on that date and also on the dates she prepared the Groens' returns, Baxter believed the Aegis trusts to be lawful.[12]

The court accepted without further question the $576,000 tax loss figure, and in May 2006 it sentenced Baxter to 24 months in prison, which was at the low end of the guidelines range.[13] Baxter unsuccessfully appealed.[14]

In August 2007 Baxter filed a motion under 28 U.S.C. section 2255 to vacate or correct her sentence. She argued (correctly) that the $576,000 tax loss amount did not relate to the false document she gave the revenue agent concerning the 1995 gain on sale of business assets — the only criminality that had been established — but instead was part of the government's $5 million-plus tax loss figure regarding the Aegis trusts — about which Baxter's criminality had not been established. Baxter maintained that her attorneys' failure to bring that fact to the court's attention resulted from their failure to hire a tax crimes sentencing expert, which constituted ineffective assistance of counsel under the Sixth Amendment.

Baxter had been represented by two attorneys, Keith Spielfogel and James Montgomery. The court emphasized:

> They each had appeared in cases before this court numerous times. This court considered, and still considers, them to be very good attorneys. Mr. Spielfogel had previously prevailed in his defense of another tax preparer in a criminal jury trial before this court, and Mr. Montgomery, who has a well-deserved national reputation as an outstanding attorney, had always previously been excellent in his representation of clients before this court.[15]

The court held an evidentiary hearing in January 2008 on Baxter's motion. At the hearing, Montgomery, "in an act that underscores his high professionalism, conceded that in hindsight his representation of Baxter was in essence constitutionally deficient as to the $576,000 tax loss figure." Spielfogel, however, denied that his representation of Baxter had been constitutionally deficient or wrong at any level. He maintained the $576,000 figure was correct.[16]

2. Sixth Amendment standards. The Sixth Amendment guarantees the right of counsel at all "critical stages" of a prosecution,[17] and the government (properly) conceded in *Baxter* that both plea and sentencing proceedings are critical stages "at which a defendant is entitled to the effective assistance of counsel."[18]

Under the Supreme Court's decision in *Strickland*, a defendant arguing ineffective assistance of counsel must establish both that the attorney's performance fell below an objective standard of reasonableness, and that it was reasonably probable that, except for the attorney's errors, the outcome of the proceedings would have been different.[19]

In the plea stage, the first of these elements entails at least three duties. Reasonably competent counsel must first endeavor to learn all pertinent facts of the case;

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[6]*Id.* at *2 and n.1.

[7]*See, e.g.*, U.S. Sentencing Guidelines Manual, section 2T1.1 comment background (1995). ("This guideline relies most heavily on the amount of loss that was the object of the offense. Tax offenses, in and of themselves, are serious offenses; however, a greater tax loss is obviously more harmful to the Treasury and more serious than a smaller one with otherwise similar characteristics. Furthermore, as the potential benefit from the offense increases, the sanction necessary to deter also increases.")

[8]*Baxter*, 2009 WL 1809927, at *2 and n.2.

[9]For discussion of presentencing reports, see Townsend et al., *supra* note 4, at 94.

[10]*Baxter*, 2009 WL 1809927, at *2.

[11]*See, e.g., United States v. Dean*, 414 F.3d 725, 730 (7th Cir. 2005).

[12]Despite being a CPA, "Baxter was gullible like hundreds of other gullible people who were duped by Aegis. . . . It was Baxter's gullibility, not greed, that guided her actions as to the Aegis system." *Baxter*, 2009 WL 1809927, at *12.

[13]*Id.* at *3.

[14]217 Fed. Appx. 557 (7th Cir.), *cert. denied*, 550 U.S. 957, *rehearing denied*, 127 S. Ct. 3038 (2007).

[15]*Baxter*, 2009 WL 1809927, at *3.

[16]*Id.*

[17]*United States v. Wade*, 388 U.S. 218, 224 (1967).

[18]*Baxter*, 2009 WL 1809927, at *4 (citing cases).

[19]*Strickland v. Washington*, 466 U.S. 668, 687-688 (1984). The second element requires "a probability sufficient to undermine confidence in the outcome."

second, analyze the applicable law to estimate the likely sentence; and third, communicate the analysis to the client.[20]

3. Application of the standard. The court concluded that Spielfogel had made sufficient efforts to learn the relevant facts. The problem was at the analytical and, derivatively, communication levels.[21]

In *Booker* the Supreme Court held that the U.S. Sentencing Guidelines violated the Sixth Amendment right to a jury trial because they allowed the sentencing judge to base a sentence on conduct that had not been found by a jury.[22] In effect, the Court made the guidelines advisory. Sentencing courts still must consider the guideline ranges, but they have flexibility to tailor sentences in light of other statutory concerns.[23]

In applying the guidelines, the sentencing court determines the appropriate base offense level under the applicable offense guideline section.[24] Regarding crimes like Baxter's, the court uses either the base offense level from section 2T4.1 (Tax Table) reflecting the tax loss, or if there is no tax loss, a base offense level of 6.[25] "The tax loss is the total amount of loss that was the object of the offense (*i.e.*, the loss that would have resulted had the offense been successfully completed)."[26] The tax loss amount is determined "on the basis of the conduct of conviction and relevant conduct; relevant conduct must be criminal or unlawful conduct," and the government must prove losses attributable to relevant conduct by a preponderance of the evidence.[27]

The court first concluded that Spielfogel's performance fell below the objective standard of reasonableness. In the court's view, "what Mr. Spielfogel seems to have done was to accept the government's position that Baxter was responsible for a $576,000 tax loss without analyzing the relationship between Baxter's conduct of conviction and the appropriate tax loss attributable to such conduct."[28] In accepting the government's position "without performing an independent analysis of the relevant sentencing provisions, Mr. Spielfogel misled both his client and the court."[29] "If Mr. Spielfogel was unwilling or unable to perform this [independent] analysis, he had a duty to engage the services of a criminal tax expert who would do so."[30]

The element of prejudice also was met. The sentencing expert Baxter retained for purposes of the section 2255 motion developed several perspectives. Among them, he testified that the $576,000 was not independent of the $5 million-plus tax loss asserted by the government but was part of it. He also testified that the tax loss from Baxter's presentation of the false document — Baxter's only established criminal conduct — was $22,853. Substituting that figure for the $576,000 and making other adjustments would produce a guidelines range of only 8 to 14 months, rather than 24 to 30 months.[31]

The court acknowledged the defendant's admissions in the plea agreement, which she could overcome only by meeting a "heavy burden of persuasion."[32] That burden was met, however. The fairness of the process in which those admissions were made was undermined by the ineffective representation the defendant received. Moreover, the court observed:

> There is no evidence that Baxter herself was qualified to assess the amount of tax loss properly attributable to her conduct for the purpose of her criminal case. Although Baxter was a CPA, she was not in a position to understand . . . the effect of the tax-loss figure on her sentencing. Rather . . . Baxter reasonably deferred to the opinion of her criminal defense attorneys regarding the application of the law to the facts of her case.[33]

The court concluded: "Had the facts and analysis that have now been presented by Baxter's tax expert, who was retained by her new counsel after her sentencing, been presented to the court prior to Baxter's 2006 sentencing, the court would have imposed a lower sentence."[34] Accordingly, the court vacated the original sentence and established a process to lead to resentencing.

C. Need a Tax Expert Be Retained in Every Case?

The *Baxter* opinion hastened to assure its readers: "Defense counsel in criminal tax cases need not always retain a tax expert to assist."[35] This is, of course, true. In many cases, counsel possesses the requisite expertise to proceed without hiring an expert.

However, three aspects of *Baxter* limit the comfort that can be drawn from the opinion's "not always necessary" language. First, as described above, Baxter's two original attorneys were not rank neophytes. They were experienced, skillful attorneys.

Second, *Baxter* was far from the most complicated sentencing puzzle. Among criminal tax cases, *Baxter* was a case of, at most, middling complexity. Post-*Booker* complexities about how rigorously or loosely to apply

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[20] *E.g.*, *Julian v. Bartley*, 495 F.3d 487, 495 (7th Cir. 2007).
[21] *Baxter*, 2009 WL 1809927, at *5-15.
[22] *United States v. Booker*, 543 U.S. 220, 230-244 (2005).
[23] *Id.* at 246-268.
[24] U.S. Sentencing Guidelines Manual, section 1B1.1(a) and (b) (1995).
[25] *Id.* at section 2T1.1(a).
[26] *Id.* at section 2T1.1(c)(1).
[27] *United States v. Frith*, 461 F.3d 914, 917 (7th Cir. 2006). Relevant conduct "includes not only the conduct for which the defendant was convicted, but also uncharged conduct, actions that took place beyond the applicable statute of limitations, actions for which the defendant was actually acquitted, and even the conduct of other people, as long as that conduct was both in furtherance of, and reasonably foreseeable in connection with, the criminal activity jointly undertaken by the defendant." Townsend et al., *supra* note 4, at 303-304; *see* U.S. Sentencing Guidelines Manual, section 1B1.3 (1995).
[28] *Baxter*, 2009 WL 1809927, at *6.
[29] *Id.* at *8.
[30] *Id.* at *6.
[31] *Id.* at *9.
[32] *Id.* at *12 (quoting *United States v. Malave*, 22 F.3d 145, 148 (7th Cir. 1994)).
[33] *Id.* at *13.
[34] *Id.* at *14.
[35] *Id.* at *11.

the sentencing guidelines were not present in the case. The principal consideration involved the amount of the tax loss, which turned on decoupling Baxter's established criminality (for the false document regarding gain on asset sale) from her established noncriminality (regarding the Aegis trusts). Only two other adjustments were present: an increase on account of Baxter's special skill,[36] and a decrease on account of her timely acceptance of responsibility.[37]

Third, the *Baxter* court stated, "Criminal tax cases involving seemingly legitimate, sophisticated tax schemes, like the Aegis Trust System . . . are among the types of cases where it is necessary that criminal defense counsel retain the assistance of a tax expert before any critical states of the defendant's criminal case occur."[38] But parties in abusive trust scheme cases do not sail uncharted seas. Abusive trust schemes have been around for generations, the IRS has clearly and repeatedly warned about them, and the government has had considerable success litigating against them.[39]

Put these aspects together. If experienced counsel in a case of roughly average sentencing complexity involving a rather well-known class of issues needs to retain tax experts to satisfy the Sixth Amendment, *Baxter* and similar cases could mean that those experts will continue to be in demand.

Criminal tax defense counsel can often do more good for their clients on sentencing than on guilt versus innocence. *Baxter* illustrates, however, that to produce those good effects, counsel must not simply accept the government's sentencing calculations. Counsel must perform an independent investigation to the best of their ability and hire a sentencing expert if that ability is limited in the circumstances of the case.

Moreover, counsel should consider retaining the expert at the start of the process, not at its end. The *Baxter* court focused on the plea and sentencing phases. However, if the government can be convinced early in the case that, in the event of conviction, the sentence imposed would be minimal, the government may decide instead to focus its limited resources on a different defendant for whom it would get more bang for its buck.

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[36]U.S. Sentencing Guidelines Manual, section 2T1.1(b)(2) (1995).

[37]*Id.* at section 3E1.1(a) and (b).

[38]*Baxter*, 2009 WL 1809927, at *14.

[39]*E.g.*, *United States v. Scott*, 37 F.3d 1564 (10th Cir. 1994), *Doc 94-9208, 94 TNT 197-40*; *United States v. Krall*, 835 F.2d 711 (8th Cir. 1987).